



# APPRAISAL BULLETIN

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## SERVICE STATION RENT

### SERVICE STATION

Basically, the service station is an investment-type property, whose value is determined 1. from the net return which can reasonably be expected during its remaining economic life; and 2. from the value of the land and reproduction cost less the depreciation accrued during its expended economic life.

The service station is a special-use retail outlet of the drive-in type, designed basically for the sale of petroleum products and some parts and accessories for the automobile and for servicing the automobile. In recent years the types of products sold have been expanding and more and more commodities of a non-motorvehicular nature are being sold at the service station. Like the drug store, it is selling goods foreign to its original purpose; such commodities as fishing tackle, electric appliances, soft drinks, cigarettes, etc., are now being sold in increasing quantities at the service station.

There are many instances in which the service station is merely a convenience or an auxiliary to some other use which provides the principal use of the land, such as a garage, parking lot, automobile sales, etc. There are other stations which are located temporarily on sites of high value in downtown sections or in buying centers where other types of commercial use would represent the highest and best use of the land. Care must be taken in all such cases to determine whether the service station represents the best use of the land before its appraisal is undertaken.

The service station is the best use of the land when the net income imputable to the land resulting from such use is greater than that from any other use and thereby creates the highest value of the land.

Like other retail outlets, the service station develops its full utility and highest rental value when the maximum volume of business possible is done, subject to the limitation of its market and the station itself.

### MARKET

The basic market of the service station is that residential neighborhood of automobile owners which is conveniently accessible to the station. The neighborhood market is the total amount of expendable income for petroleum products on a total family basis or by the number of cars in the area determined from car registration data and the calculated expenditure per car estimated upon the basis of family standard of living.

Another market source is the flow of motorvehicular traffic passing the station. Like the pedestrians passing a retail store, the flow of automobile traffic is a potential market for the service station. While these potential markets of the neighborhood and the traffic stream are quite useful in comparing the desirability of one locality with another, we have been unable to find any formulas or rules by which the volume of business of a particular station can be determined from the potential market. The four conditions which must co-exist in creating the maximum volume of business for the service station commensurate with its market and which apply to all retail outlets are:

1. The service station must be conveniently accessible to its market. There must be no barriers or hazards to ingress or egress such as too rapid flow of traffic passing the station, stop-and-go signs, etc.
2. The station must be adequate in size, equipment and personnel to handle the volume of business the market justifies, especially in peak periods.
3. The station must have competent management. Besides having the knowledge, ability and experience to direct profitable operations, the operator must be able through friendly service to retain old customers and to secure new ones.
4. Advertising of product and brand acceptance build business volume, and the quality of product and services sold must be in line with the quality of the market.

These conditions are fundamentals for all types of retail outlets and apply with equal significance in creating their maximum volume of business. When maximum volume of business is obtained, the full utility of the property is developed.

#### RENTAL VALUE

There has been little uniformity among oil companies in renting the service stations which they own to their operating managers, nor do they establish a sound basis for estimating rental value. There is a tendency among oil companies to subsidize their operators by renting company-owned stations at such low rentals that values justifying acquisition cost could only be obtained by using capitalization rates below those for any other type of investment property.

Oil companies generally use as a base in determining rental value the quantity of gasoline pumped at a unit price per gallon, with many oil companies fixing the rent on the basis of 1¢ per gallon pumped. Such a rental policy ignores the total dollar volume of business done at the station. A change in the price of gasoline or an increase in the volume of petroleum products other than gasoline and of non-petroleum products would not affect the rent paid. It is a false rent that fluctuates with the quantity of one out of many items sold at a fixed unit rent, just as if the rent of a haberdasher were based on the quantity of shirts sold at a fixed rent per shirt while the many other items which the haberdasher sells were ignored.

There can be no doubt that a rental value which would be a measure of the full utility of the service station would be a proper percentage of the maximum dollar

volume of business done at the station which includes every product and service. (See Appraisal Bulletin "The Relationship of Real Estate Rent to Business Volume.")

Due to the variety of commodities and services sold and the wide variation in the amounts of each sold at different locations, it is necessary to determine a composite percentage of rent to dollar volume of sales. The following table gives the calculations for a composite percentage for stations with below-average, average and above-average locations and market conditions.

Commodity and Service	Below Average			Average			Above Average		
	% Tot. \$ Vol.	% Rent	Comp. % Rent	% Tot. \$ Vol.	% Rent	Comp. % Rent	% Tot. \$ Vol.	% Rent	Comp. % Rent
Gasoline	90.0	5.0	4.5	75.4	5.0	3.77	55.0	5.0	2.75
Oil, grease, kerosene, etc.	6.0	5.0	0.3	8.3	5.0	0.42	12.0	5.0	0.60
Tires, batteries, accessories	2.0	8.0	0.16	9.3	8.0	0.74	15.0	8.0	1.20
Service, washing, greasing, etc.	2.0	1.0	0.02	5.0	1.0	0.05	10.0	1.0	0.10
Other	---	5.0	---	2.0	5.0	0.10	8.0	5.0	0.40
All products and services	100.0	---	4.98	100.0	---	5.08	100.0	---	5.05

It would seem that a rent of 5 per cent of the composite gross dollar volume of business represents the full measure of the utility of the service station regardless of the purchasing power of its market. Whenever special conditions increase dollar volume, such as cut-rate price of gasoline, contract with trucking company, etc., such a percentage rent would not apply.

#### APPRAISAL

The appraisal of the service station should follow the same procedure used with all commercial properties. However, the difficulty generally encountered is the unwillingness of the operating manager to give the gross volume of business so that the true rental value of the station can be estimated. This is especially the case when the manager does a large car servicing business and when large sales of automobile accessories are made independent of the station owner. In many cases the owner of the station did not know the total volume of business done by the lessee. As the rent depended upon gallonage alone, the volume of gasoline sales was of primary importance.

A recent appraisal for one of the larger oil companies included a service station which is well located in a buying center and accessible to a high-purchasing-power market and which does a total dollar volume of business of about \$90,000 per year and pumps about 260,000 gallons of gasoline per year. This station is leased to a managing operator for one year at a rental of 1¢ per gallon of gasoline pumped. The lease is renewable if found mutually agreeable to both manager and company.

In this case the rent on the basis of 5 per cent of gross volume of business is



\$4,500; on the basis of the terms of the lease of 1¢ per gallon the rent would be \$2,600. The annual rent of \$4,500 warrants a value of \$47,500 as follows:

#### Income Approach

Expected Annual Income .....		\$ 4,500
Annual Expenses, Management .....	\$ 225	
Maintenance and Repair .....	125	
Taxes .....	600	
Insurance .....	200	
Total Expense .....		<u>1,150</u>
Annual Net Income .....		\$ 3,350
Net Income Applicable to Land .....	2,250	
Net Income Applicable to Improvements .....	<u>1,100</u>	
Total .....		\$ 3,350
Value of Land - Net Income as a Perpetuity, capitalized at 6%, $\$2,250 \div .06$ .....		\$37,500
Value of Improvements, 15 Years Remaining Life, 7% Re- turn, $\$1100 \times 9.108$ .....		<u>10,000</u>
Total Value .....		\$47,500

#### Cost Approach

Value of Land, 50 feet @ \$750 .....		\$37,500
Reproduction Cost of Improvements:		
Drive and Wall .....	\$ 2,170	
Bldg. 27350 cubic feet @ 45¢ .....	12,300	
Architect's fees, financing, etc., 5.7% .....	<u>830</u>	
Maximum Value .....		<u>15,300</u>
		\$52,800
Depreciation, 34.7% .....		<u>\$ 5,300</u>
Total Value .....		\$47,500

If the rent of 1¢ per gallon as per lease were used, or \$2,600, the net income would be reduced \$1,900 and the appraised value decreased \$31,670, making the value of the land \$5,830, of the improvements, \$10,000, and the total value, \$15,830. Such a low land value cannot be justified by comparison with similar land in the locality.

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